

# Transport for the North Board Meeting – Item 7

**Subject:** Finance Update: Periods 1 & 2 Financial Year 2018/19

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**Meeting Date:** Thursday 28 June 2018

## **1. Executive Summary:**

- 1.1 This report provides a summary of the financial performance of Transport for the North over the first two months of the financial year.
- 1.2 The report compares actual expenditure in April and May to the 'base' budget. That budget was derived from a business planning process completed in January 2018, with many of the assumptions used for that exercise now require updating.
- 1.3 Over the first two months of the year, an underspend totalling £3.13m has accrued. Of this underspend, the principal driver - £3.04m (97%) – has been slipped activity. That is, planned activity that has not been progressed at the rate forecast, but which will still be undertaken.
- 1.4 This situation is most acute in Transport for the North's programme areas, and in particular within the Integrated & Smart Ticketing (IST) programme. Underspend in this programme (£2.65m) represents 85% of the overall value.
- 1.5 Material variances within the programme areas reflect both the significant planned expenditure and the sensitivity of the programmes to external issues.
- 1.6 These issues require Transport for the North to cyclically refresh its budgets to ensure that they remain relevant, supporting oversight and challenge. As part of this process, a formal refresh – known as 'Revision 1' – is underway, and a revised budget will be presented to Board for consideration at the 13th September meeting.

## **2. Recommendation:**

- 2.1 Note the year-to-date underspend of £3.13m.

- 2.2 Note that this underspend is principally driven by slipped activity within the programme areas.
- 2.3 Note that a budget refresh exercise is underway, to allow a Revision 1 estimate to be considered by Board at the meeting on 13<sup>th</sup> September.

### **3. Issues:**

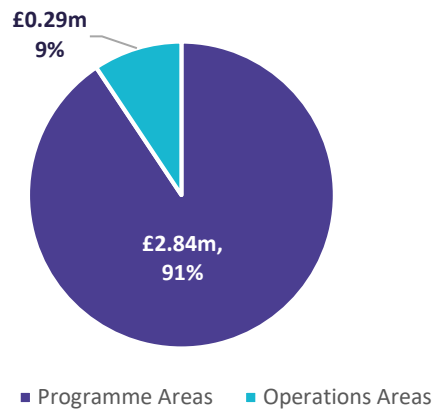
#### **Background**

- 3.1 Transport for the North's budgets consist of its major programmes of activity and the supporting work undertaken in its operations areas.
- 3.2 The major programme areas cover:
  - a) The Integrated & Smart Ticketing (IST) programme;
  - b) The Northern Powerhouse Rail (NPR) programme; and,
  - c) The Major Roads programme.
- 3.3 These programmes are differentiated from Transport for the North's operations areas for budgeting purposes to allow for better transparency over individual spending areas.
- 3.4 Programme areas have significantly more resource allocated to them than the operations areas and are often in receipt of discrete grant support. Programme area cost mixes and sensitivity to external issues also differentiate them from the more stable patterns of expenditure in the operations areas.

#### **Summary Financial Performance**

- 3.5 Over the first two periods of the new financial year (calendar months April and May) Transport for the North has spent £5.85m against its target budget of £8.98m. This means that it has underspent against the opening 'base' budget by £3.13m.
- 3.6 This underspend represents a 35% shortfall on the initial budget forecast, with underspends accruing in the programme areas accounting for 91% of the overall underspend figure:

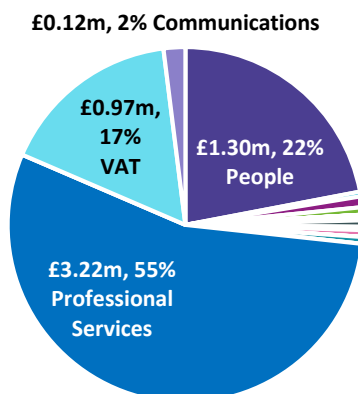
|                  | Actuals<br>£m | Budget<br>£m | Variance<br>£m | Variance<br>% |
|------------------|---------------|--------------|----------------|---------------|
| Programme Areas  | 4.54          | 7.37         | 2.84           | 38%           |
| Operations Areas | 1.32          | 1.61         | 0.29           | 18%           |
|                  | <b>5.85</b>   | <b>8.98</b>  | <b>3.13</b>    | <b>35%</b>    |



- 3.7 The principal driver of this underspend has been slipped activity. Slipped activity refers to forecast activity that has not been undertaken at the pace expected. As activity slips, the costs that had been expected to be incurred slips too. Accordingly, slippage changes the forecast timing of expenditure rather than creating sustainable savings.
- 3.8 The following table shows that slippage of £3.13m accounts for 97% of the reported underspend:

|                      | £m          | %   |
|----------------------|-------------|-----|
| Savings              | 0.09        | 3%  |
| Net Slipped Activity | 3.04        | 97% |
|                      | <b>3.13</b> |     |

- 3.9 Year-to-date cost mixes reflect that Transport for the North is principally a commissioning body.
- 3.10 Cost mixes show that majority of expenditure has been incurred on the employment of people (£1.30m year-to-date), and the engagement of professional service companies to assist with the development of the programmes and the organisation's commitment to evidence-based decision-making (£3.22m year-to-date). Notably, Transport for the North also incurs material costs on irrecoverable VAT (£0.97m year-to-date).



3.11 The following table shows cost-mix as a comparison between the actuals over periods 1 and 2 and the base budget:

|                        | Actual<br>£m | Budget<br>£m | Variance<br>£m |
|------------------------|--------------|--------------|----------------|
| Professional Services  | £3.22        | £3.74        | £0.52          |
| Capital                | £0.16        | £2.28        | £2.11          |
| Irrecoverable VAT      | £0.95        | £1.48        | £0.54          |
| People                 | £1.30        | £1.20        | -£0.10         |
| ICT                    | £0.04        | £0.10        | £0.06          |
| Stakeholder Engagement | £0.04        | £0.07        | £0.03          |
| Premises               | £0.06        | £0.06        | £0.00          |
| Travel                 | £0.03        | £0.03        | £0.01          |
| Consumables            | £0.03        | £0.02        | -£0.02         |
| Insurance              | £0.02        | £0.01        | -£0.01         |
| Banking Costs          | £0.00        | £0.00        | £0.00          |
| Recharges              | £0.00        | £0.00        | £0.00          |
| Communications         | £0.01        | £0.00        | -£0.01         |
|                        | <b>5.85</b>  | <b>8.98</b>  | <b>3.13</b>    |

3.12 The table highlights that the major variances are between costs incurred on professional services in support of the major programmes, and capital expenditure forecast for the Integrated and Smart Ticketing programme.

3.13 Underspend in these areas has an associated impact on the amount of irrecoverable VAT costs incurred. As activity slips to later in the year, the expenditure and VAT costs move with them.

### Programme Area Financial Performance

3.11 The programme areas relate to Transport for the North's major spheres of activity. In budgetary terms, the programme areas are also

the largest spending areas, accounting for £69.80m or 87% of the overall budget for the year.

3.12 Over periods 1 & 2, expenditure in the programme areas amounted to £4.54m, £2.84m (38%) behind the budgeted expenditure level of £7.37m.

3.13 The principal source of this underspend is the Integrated & Smart Ticketing programme, with additional underspend in the Major Roads programme partially offset by marginal cost accelerations on the Northern Powerhouse Rail programme:

|                              | Actuals<br>£m | Budget<br>£m | Variance<br>£m | Variance<br>% |
|------------------------------|---------------|--------------|----------------|---------------|
| Integrated & Smart Ticketing | 1.15          | 3.80         | 2.65           | 70%           |
| Northern Powerhouse Rail     | 2.99          | 2.89         | -0.10          | -4%           |
| Major Roads                  | 0.40          | 0.69         | 0.29           | 42%           |
|                              | <b>4.54</b>   | <b>7.37</b>  | <b>2.84</b>    | <b>38%</b>    |

3.14 Underspend in the Integrated and Smart Ticketing programme is primarily due to the effects of delays that were experienced in the last financial year. These delays have led to the base budget expenditure profiles being largely out-dated, and misaligned to new timelines the programme is working to.

3.15 In the previous financial year delays to the conclusion of Franchise Side Agreements between Transport for the North (and its contracting partners) and the train operating companies (TOCs) pushed the timeline for the delivery of the ITSO on Rail Phase 1 project back by several months. The forecast included in the base budget assumed that by this stage the TOCs would be incurring significant expenditure on the procurement and integration of new equipment. Delays to contracting, now largely resolved, have pushed the main body of this activity back beyond Period 2.

3.16 Phase 1 issues have been compounded by the delays to the passage of the Phase 3 project through the Department for Transport's outline business case (OBC) gateway. That issue, along with a need for engagement with the Government Digital Service (GDS) has had a material impact upon the programme's activity plans, and associated expenditure profiles.

3.17 Work is underway to realign expenditure profiles to the programme's delivery plan as part of the Revision 1 budget refresh exercise. Although it is expected that the Phase 1 activity will catch-up within the financial year, it is likely that some Phase 3 activity will slip into financial year 2019/20.

- 3.18 Underspend has also accrued in the Major Roads programme (£0.29m), where work is underway to deliver the Strategic Development Corridor (SDC) studies. These studies are complemented by a number of ancillary modelling and economic appraisal studies, which will support the evidence base.
- 3.19 Delays to the delivery of those modelling studies, due to the complexity of the activity and capacity constraints, stretch back to the final quarter of the previous financial year. This has had a knock-on impact on the overall SDC studies, with expenditure levels falling behind profile. It is expected that this activity will catch-up in the coming months.
- 3.20 The Northern Powerhouse Rail programme shows an acceleration of costs ahead of profile (£0.10m) as activity advances towards the delivery of the strategic outline business case (SOBC) in the autumn.
- 3.21 These accelerations principally relate to the work undertaken by Network Rail on the Sequence 3 Phase 2 studies in support of the SOBC. Accelerations here offset some slippage on works around the HS2/NPR station study work packages.
- 3.21 Cost accelerations of this kind are monitored carefully with the programme management leads to ensure that cash flow matters are considered and that increased cash flow represents acceleration of activity rather than cost increases *per se*.

### Operations Area Financial Performance

- 3.22 Transport for the North's operations area cover the back, middle, and front office functions familiar to any public body organisation. These teams discharge the statutory functions of the business, and support programme delivery.
- 3.33 Over periods 1 and 2 of the new financial year, the operations areas incurred expenditure of £1.32m against a budget of £1.61m, leading to an underspend of £0.29m (18%):

|                             | Actual<br>£m | Budget<br>£m | Variance<br>£m | Variance<br>% |
|-----------------------------|--------------|--------------|----------------|---------------|
| Leadership                  | 0.05         | 0.05         | -              | -5%           |
| Finance                     | 0.16         | 0.16         | -              | -2%           |
| Business Capabilities       | 0.51         | 0.65         | 0.14           | 22%           |
| Programme Management Office | 0.05         | 0.11         | 0.06           | 56%           |
| Strategy & Policy           | 0.25         | 0.37         | 0.13           | 34%           |
| Rail North                  | 0.30         | 0.26         | (0.04)         | -14%          |
|                             | <b>1.32</b>  | <b>1.61</b>  | <b>0.29</b>    |               |

- 3.34 The majority of the underspend within the Strategy and Policy team relates to professional services lines. This reflects slippage in modelling and appraisal studies (£0.08m) but also lower costs incurred on the Strategic Transport Plan (STP) consultation (£0.02m) - the latter reflecting the a prudent budgetary provision that was made to cover the incremental costs of managing varying volumes of consultation response.
- 3.35 The Business Capabilities team covers many of the back-office functions including Legal, HR, ICT, and office accommodation. The underspend in this area includes underspend against the learning and training budget (£0.03m) and underspends within the ICT budget (£0.07m).
- 3.36 The latter issue reflects a technical budgetary change in assumptions around the costs of Transport for the North's back-office enterprise resource planning system (ERP). Adjustments will be made to the budget to reflect this change as part of the Revision 1 budget refresh.
- 3.37 Spend ahead of budget in the Rail North area reflects slipped activity that commenced at the end of March 2018 falling into the new financial year. This activity is un-budgeted in 2018/19 as it had been envisaged that the work would have been completed in 2017/18. However, whilst the activity has slipped into 2018/19, the resource remains available to complete this activity now, and a formal request to 'carry-forward' the resource and adjust the budget ceiling will be brought to the TfN Board at the September meeting.

### Income

- 3.38 TfN is funded principally through grant received from the Department for Transport. Over periods 1 and 2 grant was drawn upon to resource the £5.83m of expenditure:

| Funding                           | £m          |
|-----------------------------------|-------------|
| Core Grant                        | 1.72        |
| Transport Development Fund - Rail | 2.86        |
| Rail North Grant & Contributions  | 0.16        |
| IST - Revenue                     | 0.43        |
| IST - Capital                     | 0.68        |
|                                   | <b>5.85</b> |

### Cash Position

- 3.39 Transport for the North started the financial year with £15.41m of cash at bank. Since that point, the Department for Transport for has advanced funds in relation to activity for the new financial year (£13m), whilst cash payments of £5.73m have been made.

- 3.40 At the close of Period 2, Transport for the North retained £22.66m cash at the bank, which after cash it set aside for existing obligations leaves £16.22m of uncommitted resource:

|                                | £m           |
|--------------------------------|--------------|
| <b>Opening Cash Position</b>   | <b>15.41</b> |
| + Cash Received                | 13.00        |
| - Payments Made                | - 5.73       |
| <b>= Closing Cash Position</b> | <b>22.68</b> |
| - Accrued Expenditure*         | - 6.44       |
| <b>= Net Available Cash</b>    | <b>16.24</b> |

*\*including expenditure accrued in 2017/18*

- 3.41 This resource is earmarked to resource part of this financial year's budget (£80.03m) and Transport for the North's target year-end cash reserve balance of £3m. The value is also elevated by year-end slippage of £2.29m.
- 3.42 A request for the 'carry-forward' of this slipped resource into the new financial year will be made to TfN Board after review by the Scrutiny Committee.
- 3.43 Transport for the North finance officers meet regularly with Department for Transport colleagues to discuss cash requirements.

#### **4. Options Considered:**

- 4.1 This paper is a backward look at the financial performance of Transport for the North over periods 1 and 2 of the new financial year. It does not offer any recommendations for action.

#### **5. Considerations:**

- 5.1 This paper does not offer any recommendations for actions.

#### **6. Preferred Option:**

- 6.1 This paper does not offer any recommendations for actions.

#### **Appendices:**

None.



## List of Background Documents

### Required Considerations

*Please confirm using the yes/no options whether or not the following considerations are of relevance to this report.*

#### Equalities:

|                         |                |    |
|-------------------------|----------------|----|
| Age                     | <del>Yes</del> | No |
| Disability              | Yes            | No |
| Gender Reassignment     | Yes            | No |
| Pregnancy and Maternity | Yes            | No |
| Race                    | Yes            | No |
| Religion or Belief      | Yes            | No |
| Sex                     | Yes            | No |
| Sexual Orientation      | Yes            | No |

#### Environment and Sustainability

|                |    |
|----------------|----|
| <del>Yes</del> | No |
|----------------|----|

|              |     |               |
|--------------|-----|---------------|
| Legal        | Yes | No            |
| Financial    | Yes | <del>No</del> |
| Resource     | Yes | <del>No</del> |
| Risk         | Yes | <del>No</del> |
| Consultation | Yes | <del>No</del> |